COMMITTEE ON FINANCE
NEWS RELEASE
Max Baucus, Chairman
http://finance.senate.gov

For Immediate Release
October 19, 2007

Contact: Carol Guthrie
202-224-4515

Statement of Senator Max Baucus (D-Mont.)
Regarding The Research Competitiveness Act of 2007

Mr. President, back in 1962, Marshall McLuhan wrote, "The new electronic interdependence recreates the world in the image of a global village." Certainly, 40 years later, that concept is truer than ever. As we prepare for the future in this global village, we need to affirm America's leadership role in the world.

The United States accounts for one-third of the world's spending on scientific research and development, ranking first among all countries. While this is impressive, relative to GDP, though, America falls to sixth place. And the trends show that maintaining American leadership in the future depends on increased commitment to research and science.

Asia has recognized this. Asia is plowing more funding into science and education. China, in particular, understands that technological advancement means security, independence, and economic growth. Spending on research and development has increased by 140 percent in China, Korea, and Taiwan. In America, it has increased by only 34 percent.

Asia's commitment is already paying off. More than a hundred Fortune 500 companies have opened research centers in India and China. I have visited some of them. I was impressed with the level of skill of the workers whom I met there.

China's commitment to research, at $60 billion in expenditures, is dramatic by any measure. Over the last few years, China has doubled the share of its economy that it invests in research. China intends to double the amount committed to basic research in the next decade. Currently, only America beats out China in numbers of researchers in the workforce.

Today, I am pleased to join with my Colleague on the Finance Committee, Senator Hatch, to introduce the Research Competitiveness Act of 2007. This bill would improve our research competitiveness in four major areas. All four address incentives in our tax code. Government also supports research through federal spending. But I am not addressing those areas today.

First, our bill improves and simplifies the credit for applied research in section 41 of the tax code. This credit has grown to be overly complex, both for taxpayers and the IRS. Beginning in 2008, our bill would create a simpler credit for qualifying research expenses that exceed 50 percent of the average expenses for the prior three years. This simplified credit would phase in over three years.

And just as important, the bill makes the credit permanent. Because the credit has been temporary, it has simply not been as effective as it could be. Since its creation in 1981, it has been extended 11 times. Congress even allowed it to lapse during one period.

--2 more--

The credit last expired in December of 2005. After much consternation and delay, Congress passed a two-year extension of the credit for 2006 and 2007. These temporary extensions have taken their toll on taxpayers. In 2005, the experts at the Joint Committee on Taxation wrote: "Perhaps the greatest criticism of the R&E credit among taxpayers regards its temporary nature." Joint Tax went on to say, "A credit of longer duration may more successfully induce additional research than would a temporary credit, even if the temporary credit is periodically renewed."

Currently, there are three different ways to claim a tax credit for qualifying research expenses. First, the "traditional" credit relies on incremental increases in expenses compared to a mid-1980s base period. Second, the "alternative incremental" credit measures the increase in research over the average of the prior four years.

Both of these credits have base periods involving gross receipts. Under the new tax bill enacted last month, a third formula was created, which does not rely on gross receipts and is available only for 2007. Our bill simplifies these credits and will move all taxpayers to the "Alternative Simplified Credit," which is based on research spending without reference to gross receipts. The current formulas hurt companies that have fluctuating sales. And it hurts companies that take on a new line of business not dependent on research.

This new simpler formula in our bill would not start until 2008. That start date would give companies plenty of time to adjust their accounting. The current formula would be available to companies for two years, and then it would phase out.

The main complaint about the existing credits is that they are very complex, particularly the reference to the 20-year-old base period. This base period creates problems for the taxpayer in trying to calculate the credit. And it creates problems for the IRS in trying to administer and audit those claims.

The new credit focuses only on expenses, not gross receipts. And it is still an incremental credit, so that companies must continue to increase research spending over time. Further, this bill adds a mandate for a Treasury study to look at substantiation issues and ensure that current recordkeeping requirements assist the IRS without unduly burdening the taxpayer.

A tax credit is a cost-effective way to promote R&E. A report by the Congressional Research Service finds that without government support, investment in R&E would fall short of the socially optimal amount. Thus CRS endorses Government policies to boost private sector R&E. Also, American workers who are engaged in R&E activities benefit from some of the most intellectually stimulating, high-paying, high-skilled jobs in the economy.

My own State of Montana has excellent examples of this economic activity. During the 1990s, about 400 establishments in Montana provided high-technology services, at an average wage of about $35,000 per year. These jobs paid nearly 80 percent more than the average private sector wage, which was less than $20,000 a year during the same period. Many of these jobs would never have been created without the assistance of the R&E credit.

Our research bill would also establish a uniform reimbursement rate for all contract and consortia R&E. It would provide that 80 percent of expenses for research performed for the taxpayer by other parties count as qualifying research expenses under the regular credit.

--1 more--

Currently, when a taxpayer pays someone else to perform research for the taxpayer, the taxpayer can claim one of three rates in order to determine how much the taxpayer can include for the research credit. The lower amount is meant to assure overhead expenses that normally do not qualify for the R&E credit are not counted. Different rates, however, create unnecessary complexity. Therefore, our bill creates a uniform rate of 80 percent.

The second major research area that this bill addresses is the need to enhance and simplify the credit for basic research. This credit benefits universities and other entities committed to basic research. And it benefits the companies or individuals who donate to them. Our bill provides that payments under the university basic research credit would count as contractor expenses at the rate of 100 percent.

The current formula for calculating the university basic research credit — defined as research "for the advancement of science with no specific commercial objective"— is even more complex that the regular traditional R&E credit. Because of this complexity, this credit costs less than one-half of 1 percent of the cost of the regular R&E credit. It is completely under-utilized. It needs to be simplified to encourage businesses to give more for basic research.

American universities have been powerful engines of scientific discovery. To maintain our premier global position in basic research, America relies on sustained high levels of basic research funding and the ability to recruit the most talented students in the world. The gestation of scientific discovery is long. At least at first, we cannot know the commercial applications of a discovery. But America leads the world in biotechnology today because of support for basic research in chemistry and physics in the 1960s. Maintaining a commitment to scientific inquiry, therefore, must be part of our vision for sustained competitiveness.

Translating university discoveries into commercial products also takes innovation, capital, and risk. The Center for Strategic and International Studies asked what kind of government intervention can maintain technological leadership. One source of technological innovation that provides America with comparative advantage is the combination of university research programs, entrepreneurs, and risk capital from venture capitalists, corporations, or governments. Research clusters around Silicon Valley and North Carolina's Research Triangle exemplify this sort of combination.

The National Academies reached a similar conclusion in a 2002 review of the National Nanotechnology Initiatives. In a report, they wrote: "To enhance the transition from basic to applied research, the committee recommends that industrial partnerships be stimulated and nurtured to help accelerate the commercialization of national nanotechnology developments."

In sum, our bill would boost both applied and basic research. It would boost research by businesses big and small. And it would foster research by for-profit and non-profits alike.

McLuhan's quote about the global village was taken by many at the time as a wake-up call to a changing world. Since then, many more leaders in this village have emerged. Let us work to see that the next big technological advance is discovered here in America. Only through continued commitment to research can we ensure that it is.

Mr. President, I ask unanimous consent that a copy of the bill be printed in the Record at this point.

###